



Early Journal Content on JSTOR, Free to Anyone in the World

This article is one of nearly 500,000 scholarly works digitized and made freely available to everyone in the world by JSTOR.

Known as the Early Journal Content, this set of works include research articles, news, letters, and other writings published in more than 200 of the oldest leading academic journals. The works date from the mid-seventeenth to the early twentieth centuries.

We encourage people to read and share the Early Journal Content openly and to tell others that this resource exists. People may post this content online or redistribute in any way for non-commercial purposes.

Read more about Early Journal Content at <http://about.jstor.org/participate-jstor/individuals/early-journal-content>.

JSTOR is a digital library of academic journals, books, and primary source objects. JSTOR helps people discover, use, and build upon a wide range of content through a powerful research and teaching platform, and preserves this content for future generations. JSTOR is part of ITHAKA, a not-for-profit organization that also includes Ithaka S+R and Portico. For more information about JSTOR, please contact support@jstor.org.

THE JOURNAL OF POLITICAL ECONOMY

VOLUME 18

OCTOBER—1910

NUMBER 8

SHALL RAILWAY PROFITS BE LIMITED?

Unless all signs fail, the phase of the “railway problem” which will occupy the largest place in the public mind and in public discussion for some years is the question whether railway profits shall be limited; and if so, how and to what extent. Both the Interstate Commerce act and various statute laws prohibit railway rates which are “unduly discriminatory” or “unjust and unreasonable,” the latter phrase meaning, where used, excessive—exorbitant. Everyone agrees that these are salutary provisions. It is commonly assumed that large profits result from high rates. It is therefore concluded by many that to keep rates from being exorbitant railway profits must and should be restricted.

This theory has been voiced in many quarters. Mr. Geo. A. Rankin, in a recent book,¹ advocates concentrating the control of all the railways of the United States in one holding corporation limited to a net return of 5 per cent. In many proceedings before railway commissions and courts the same doctrine that the public may and therefore ought to restrict each railway to a “fair return” is being urged by those who favor reductions of rates by action of public authorities or who oppose advances in rates sought by the railways. Efforts are being made to secure the passing of legislation which will establish the principle of limitation of profits and provide special machinery for carrying

¹ *An American Railway Transportation System: A Criticism of the Past and Present and a Plan for the Future.*

it out. The plan to have the Interstate Commerce Commission make a valuation of all the railways, which plan was approved by the House of Representatives at the last session of Congress but rejected by the Senate, is advocated on the ground that the roads should be restricted to a "fair return," and that what is a "fair return" cannot be known without ascertaining the value of their properties. Typical of many bills introduced in the last Congress was that of Representative William R. Smith of Texas. This bill would have required the Commission to fix all interstate rates so that they would "yield only a reasonable net return on a fair value of the carrier's property as determined by the Commission."

If it were indisputable that limitation of profits is necessarily involved in fixing fair and reasonable rates, no one, perhaps, would question the constitutionality or expediency of the proposed policy. But railway counsel and managers, and some competent students of railway affairs, contend that limitation of profits is not necessarily involved in just and effective regulation of rates, but is a different and even antagonistic policy. The cornerstone of the theory that limitation of profits is essential to effective regulation of rates is the assumption that there is a fixed causal relation between rates and profits owing to which they rise and fall together. Now this is not true. It is true that a railway with high rates may earn large profits, and that a railway with low rates may earn small profits. But it is also true that a railway with low rates may earn large profits and that one with high rates may earn small profits. The average rate per ton per mile of the Central of Georgia in 1909 was almost 11 mills and its net earnings per mile were \$1,500, while the average rate per ton per mile of the Lake Shore & Michigan Southern was only a little over 5 mills, and its net earnings per mile were \$9,350. It is true that raising rates may increase profits and that a reduction of rates may reduce profits. But raising rates may reduce profits and a reduction of rates may cause, or at least be accompanied by, an increase of profits. Which result will follow always depends on the effect upon the volume of the traffic. The average rate per ton per mile in the

United States declined from 9.41 mills in 1890 to 7.59 mills in 1907, or 24 per cent.; and meantime the average net earnings of the railways of the country increased from \$2,300 to \$3,696 per mile, or 60 per cent.

The profits of a railway are affected by many factors of which the amount of the rate is but one. Profits are the difference between gross earnings and expenses. Gross earnings depend on the nature and density of the traffic as well as on the rates applied to it. Expenses, both in the aggregate and per unit of traffic, depend on how much and what kind of traffic is handled, on what kind of a territory it is hauled through, and on what kind of a management the railway has. Of two roads handling the same kind of traffic, between the same points, on the same rates, one may have very large net earnings and the other only small net earnings or even none. If we are to use profits as the test of the reasonableness of rates, shall we say in such cases that the rates are unreasonably high or unreasonably low? A road might be earning more than a "fair return." Its rates on the theory under consideration would be held unreasonable. By advancing them it might destroy enough traffic to reduce its earnings to a "fair return." Would it thereby make its rates reasonable? A road might be earning exactly a "fair return." By a reduction in its rates, causing a large increase in its traffic, or by improvements in its plant or by methods causing reductions in its operating expenses, it might raise its net earnings above a "fair return." Would this *reduction* in its rates, or this improvement in its plant or methods, make the rates of this road unreasonable?

The foregoing considerations show that limiting profits is really quite a distinct thing from requiring reasonable rates. The constitutionality and expediency of legislation to limit profits must, therefore, be defended on other grounds than that of regulation to secure fair and reasonable rates.

Many persons, including most railway commissioners and numerous lawyers, think that it has been settled by decisions of the Supreme Court of the United States that the profits of railways may be limited. Mr. Justice Harlan said in the opinion

of the court in the Nebraska Rate Case² that "what the [railway] company is entitled to earn is a fair return on the fair value of that which it employs for the public convenience." This is interpreted to mean that a "fair return" is *all* to which a railway is entitled. It is argued that the "fair value" of the property is that for which it could be physically reproduced, and that a "fair return" is the current rate of interest on good securities. It is therefore concluded that a valuation of the properties of railways should be made, and that rates should then be so adjusted from time to time that each road will earn only the current rate of interest on its valuation.

Counsel for the railways and some able constitutional lawyers repudiate this interpretation of Justice Harlan's statement.³ Justice Harlan did not say that all the railway company is entitled to demand is a fair return, but that this is the least to which it is entitled. That he did not mean that this is the maximum which it may be entitled to receive is indicated by a statement made four years later by Justice Brewer in rendering the opinion in *Cotting v. Godard*.⁴

As to parties engaged in a public service, while the power to regulate has been sustained, negatively the [supreme] court has held that the legislature may not prescribe rates which, if enforced, would amount to a confiscation of property. *But it has not held that the legislature may enforce rates that stop only this side of confiscation.*

This shows that the court had not up to that time held that railway profits might be limited; and it has not so held since. What, then, would it probably hold if the point were squarely presented to it? Whether it would sustain an order of a state or of the Interstate Commission requiring railways to reduce their rates expressly because their profits exceeded a fair return would, no doubt, depend on its construction of the statute under

² *Smyth v. Ames*, 169 U.S. 466, decided in 1897.

³ See, for example, an address by Walker D. Hines, chairman of the Executive Committee and general counsel of the Atchison, Topeka & Santa Fé, before the Traffic Club of Pittsburgh, March 18, 1910. Also an address by United States Senator W. J. Bailey of Texas, eminent as a constitutional lawyer, before the New York Bar Association, January 20, 1910.

⁴ 183 U.S. 75.

which the Commission acted. The Interstate Commerce act as amended by the Hepburn and the recent Mann-Elkins acts provides that after the Interstate Commission shall find a rate unduly discriminatory or unreasonable, it shall "determine and prescribe what will be the just and reasonable rate to be thereafter observed in such case as the *maximum* to be charged." Now, the minimum rate a railway can ever reasonably accept is one which will develop traffic that will add a little more to its earnings than to its expenses. If the traffic developed adds \$100 to expenses and but \$99 to earnings, obviously the rate is lower than the railway can reasonably accept. The maximum rate a railway can ever reasonably charge is one which falls a little short of the value of the service rendered for it. If 100 pounds of a commodity are worth \$1 in A and \$1.25 in B, and the rate per 100 pounds from A to B is 25 cents, the owner will gain nothing by shipping it from A to B. But if the rate be but 20 cents it will cost a little less than the value of the service rendered by transporting the commodity from A to B; and the owner can ship it at a profit. Now, railway counsel argue, in view of these facts it is evident that what the Interstate Commerce act means is that the Commission cannot reduce a rate, no matter what profits the railway is making, unless the rate exceeds the maximum reasonable value of the service rendered for the rate—in other words, is extortionate. In support of this view they call attention to the fact that when the Hepburn bill was pending it was proposed to give the Commission authority to fix absolute rates, and that it was also proposed to empower it to fix minimum as well as maximum rates. Both these propositions were rejected, because Congress thought it might be desirable in some cases for the railways to make lower rates than those fixed by the Commission. But it cannot be assumed that Congress meant to encourage the railways to make any rates unreasonably low. It must follow that it meant that the Commission should fix not rates which would limit railway profits to a "fair return" but merely rates which would relieve and protect shippers and travelers from unfair discrimination or extortion.

It is probable that to get finally settled the question whether rates may constitutionally be so regulated as to limit railway profits a case will have to go to the Supreme Court involving the validity of a law expressly providing for this as is done in the bill of Representative Smith above referred to. Most railway commissions and many lawyers believe such a law would be upheld. For, they reason, the railway is engaged in a public service; it exercises the power of eminent domain; and therefore Congress and the state legislatures, or commissions to which they delegate the requisite power, may regulate its charges in any way they believe for the public good, so long as they do not contravene those provisions of the fifth and fourteenth amendments to the federal Constitution which prohibit confiscation of property. Many railway lawyers and other persons who have studied the subject reject this view. They believe there are limitations on the power to regulate public service concerns besides those imposed by the fifth and fourteenth amendments. The authority of the states to regulate rates is a police power derived from the common law. The power of Congress to regulate them is derived from the Interstate Commerce clause of the federal Constitution, which, like other parts of the Constitution, must be interpreted in the light of the common law.⁵ Now, it never was the law that the *profits* of one engaged in a public service could be limited. Justice Brewer in *Cotting v. Godard*⁶ defined the rule of the common law to be that the person who engaged in a public service had "a right to charge for each separate service that which was a reasonable compensation therefor." If a shipper thought a carrier had charged him an exorbitant rate he might sue the carrier to recover the excessive portion. The court then determined whether the charge was reasonable, not by computing how much profit the carrier was making from its entire business, but by ascertaining what the particular service was worth by reference to the skill with

⁵ "The code of constitutional and statutory construction which is constantly formed by the federal courts in the application of the Constitution and laws, and treaties made in pursuance thereof, has for its basis the common law."—*Cyclopedia of Law and Procedure*, VIII, 386.

⁶ 183 U.S. 75, decided in 1901, four years after *Smyth v. Ames*.

which the service was rendered, its value to the shipper, what was customarily paid for like services under similar conditions, etc. Justice Brewer in the opinion in *Cotting v. Godard* indicated that the common-law rule was still in effect, and could not be abrogated by statute. He said:

Its [the legislature's] prescription of rates is prima facie evidence of their reasonableness. . . . But it does not follow therefore that the legislature has power to reduce any reasonable charges because by reason of the volume of business done by the party he is making more profit than others in the same business. The question is always, not what does he make as the aggregate of his profits, but what is the value of the services he renders to the one seeking and receiving the service. . . . The amount of the aggregate profits may be a factor in considering the reasonableness of the charges, but it is only one factor, and is not that which finally determines the question of reasonableness.

As the decision in this case turned on other points than the reasonableness *per se* of the rates involved, these remarks of Justice Brewer are regarded as *obiter dicta*; but his statement that legislatures cannot reduce charges conforming to the common-law standard of reasonableness merely because a concern's profits are large is significant. Of course, if a legislature cannot do this, a commission cannot.

In other cases the Supreme Court has indicated that there are limitations on the power of public authorities to regulate railways besides those which prohibit confiscation. In the case of *Monongahela Navigation Company v. U.S.*⁷ which was decided some years before *Cotting v. Godard*, the court said:

For each separate use of one's property by others the owner is entitled to a reasonable compensation; and the number of such uses determines the productiveness and earnings of the property, and therefore largely its value.

In *Railroad Company v. Smith*,⁸ speaking of the property right of railways in the management of their affairs, it said:

What the company may choose voluntarily to do furnishes no criterion for the measurement of the power of a legislature. Persons may voluntarily contract to do what no legislature would have the right to compel them to do.

⁷ 158 U.S. 312.

⁸ 173 U.S. 684.

And in the recent case of *Interstate Commerce Commission v. C. G. W. Ry.*,⁹ which arose under the Elkins law, and was decided after the Hepburn act was passed, it said:

It must be remembered that railroads are the private property of their owners; that while from the public character of the work in which they are engaged the public has the power to prescribe rules for securing faithful and efficient service and equality between shippers and communities, yet in no proper sense is the public a general manager.

Those who think that railway profits cannot be limited construe these statements to mean that public authorities may so regulate railways as to require them to give the public good and adequate service at fair and reasonable rates; but that if they go farther than this, and seek to direct the internal management of the railways and to say what profits they may earn and what dividends they may pay, they encroach on the private side of the carriers and invade prerogatives and rights which the Constitution, so long as the carriers continue to be private property, reserves to their owners and managers.

Many persons will think that if this is the correct view the situation is unfortunate, and that the Constitution should be so amended as specifically to empower and require public authorities to restrict railways to an average return approximating the current rate of interest on either their cash investments or the value of their physical properties. It is contended that as railway corporations are created by, derive all their power from, and in maintaining a public highway, exercise a function of, the state, the public has a right to limit their profits.

The question of most importance after all, however, is not what the public has a legal or an abstract moral right to do, but what it is to its interest to do. If it is reasonably sure to inure to the good of the public to limit railway earnings as proposed, this limitation ought to be made. The interest of the public is superior to all other considerations. But when we consider all that would be involved in carrying out the policy of limitation of railway profits in the way that is advocated, and when we consider all the effects that this policy would probably pro-

⁹ 209 U.S. 108.

duce, it may be doubted whether the majority will regard it as expedient.

Regulation of railways should aim to secure three main objects: (1) safe, good, and adequate transportation; (2) rates which do not unfairly discriminate; and (3) the lowest rates compatible with good service. The criterion of the expediency of any policy is the way in which it is adapted to attaining these ends.

To carry out effectively the proposed policy of regulation through limitation of profits would require extension of regulation to almost every detail of the railway business. The Supreme Court has said that the public is in no proper sense the general manager of the railways. It would have to become their general manager to carry out this policy. The railway commissions would have to be authorized to fix the basis, or valuation, on which a return might be earned, and also the percentage of return to be allowed. Then they would have to exercise absolute control over railway accounting. For each road constantly spends money for maintenance of equipment, track, etc., and also for permanent improvements. Now, maintenance is chargeable to operating expenses, while permanent improvements are chargeable to capital account; new securities entitled to the "fair return" could be issued against them. But as to just where expenditures for maintenance end and expenditures for permanent improvements begin expert opinions differ. The railway managements, desiring to build as broad a basis of valuation and capitalization as possible, would be disposed to charge all of the expenditures within this "twilight zone" to permanent improvements; and to prevent them from unreasonably swelling their capitalizations railway commissions would have to be empowered to determine to what account each item of expenditure should be charged.

Again, profits are the margin between earnings and expenses. The management of a railway, seeing that its profits were about to pass the limit of a "fair return," might prefer to check their growth by unnecessarily increasing its expenses rather than by reducing its rates. To prevent the railways from

thus anticipating the government in limiting their profits commissions probably would have to be given authority to say what salaries should be paid by them, what prices they should pay for materials—in short, to control their expenditures as thoroughly as their rates.

It is sometimes said that if the dividends railways might pay were limited they would invest their surplus profits in permanent improvements and extensions; and that more adequate and efficient facilities of transportation would result. It is not uncommon now for a road to earn 10, 15, or even 20 per cent. annually, and to pay out in dividends only 6 or 8 per cent., the surplus earnings being spent on extensions and improvements. This, it is said, is clearly more to the interest of the public than for a road to pay out its entire net earnings annually to its security holders; and if all railways were required to pursue a similar policy the public would benefit greatly. But railways do not voluntarily limit the *profits* that they earn. They merely limit the amount of their profits that they pay out in *dividends*. And they do not limit the amount that they pay out in dividends because they think the stockholders ought not to have more, but because they desire, by investing part of past earnings in the improvement of the plants, to give the public safer and better service, and to maintain or increase the earning capacity of the roads so as to enable them in the long run to pay the stockholders more than they could if improvements were not made out of earnings. Now, under a policy of governmental limitation of profits, not the dividends, but the *net earnings*, of each railway would be restricted to the current rate of interest. Consequently, unless a company refused to pay its stockholders the current rate of interest it could not have any surplus earnings to invest in improvements; and if its earnings equaled the current rate of interest it would not withhold any of them to invest in improvements, because no doubt the main object of a railway in investing earnings in improvements is to increase profits, and no increase of profits would be allowed.

The principal purposes of improvements in methods of operation are the same as those of improvements in industrial plants, viz., to give the public better service and to reduce oper-

ating expenses, and thereby increase profits. As under the proposed policy no increase in profits exceeding the current rate of interest would be allowed, there apparently would be, after net earnings reached that point, as little incentive for the management to improve its operating methods as to improve its plant. In fact, there would be a deterrent to attempting improvements. At present improvements are undertaken with the hope of increasing profits, but always with the knowledge that their cost may turn out to exceed their worth. Under the proposed policy, if an attempted improvement turned out unprofitably the road would have to bear the loss; while if it turned out well, the benefit would go, not to the railway's stockholders in the form of increased dividends, but to shippers and travelers in the form of reduced rates.

So it would seem that the enterprise, initiative, and plans for making improvements in plants and methods in order to reduce the expenses of operation would have to be supplied by railway commissions, which would have to be given large power and discretion to coerce inert and refractory railway managements along the path of progress. It will be hard for most persons to believe that under this plan the development and improvement of transportation facilities would go on as rapidly and cheaply as in the past. Public commissions, however intelligent and powerful, hardly could get railway managers and owners to make as great improvements as they make voluntarily under the stimulus of the desire and expectation of gain.

Another consequence of this policy would be the necessity of obtaining in the money market in the form of new capital all the financial means for making permanent improvements in our railways. This, if it could be done, would probably result in a rapid increase in railway capitalization. English railways have followed this method in making their permanent improvements, and this is one of the main reasons why they are capitalized for \$314,000 a mile, while the net capitalization of the railways of the United States is but \$57,230 a mile.¹⁰

¹⁰ *Twenty-third Annual Report of the Interstate Commerce Commission* (for 1908), 61.

But could these financial means be secured in the money market? If railway capital were to be both limited to, and *guaranteed*, the current rate of interest, plenty could be obtained. But those who advocate limiting profits repudiate suggestions that the maximum return fixed by the public shall also be guaranteed by the public as a minimum. Can it reasonably be expected that capitalists would invest billions in railways knowing that they would have only a very restricted control over their property and would not be allowed more than the current rate of interest and might receive less or even nothing?

Let us now consider what effects the proposed policy would have on rates. It would not help to eliminate unfair discriminations. For discrimination consists entirely in the *relation* of rates. A road all of whose rates are low and which is not earning its operating expenses can discriminate just as unlawfully and perniciously as one that is enormously prosperous. Discrimination being entirely a matter of the relation of rates, it can only be corrected by changing their relation. While limitation of profits would not help to remove or prevent discriminations it is conceivable that it might sometimes have the opposite effect. Suppose a community alleged that a railway which was earning exactly a "fair return" was discriminating against it. The commission could not reduce the rates of the complaining community, because that might reduce the earnings of the railway below a "fair return." It could not raise the rates of the favored community because no existing law gives a commission power to raise a rate. And the road could not raise its rates to the favored community because that might increase its profits above a "fair return." How, then, could the discrimination be corrected?

It is commonly assumed that limitation of profits would tend to make rates low. This is the main reason why it is advocated. The average rate per ton per mile in the United States in 1870 was 20 mills. In 1887, when the Interstate Commerce act was passed, it had been reduced to 13 mills, or 48 per cent. Between 1887 and 1906, in which latter year the Hepburn act went into effect, it declined from 13 mills to 7.48 mills, or 42

per cent. Government regulation had no hand in the great and innumerable reductions prior to 1887 reflected in the decline in the average rate. They were made by the traffic managers of the railways. It had very little hand in the great and innumerable reductions in the period 1887-1906. Practically all were made by the traffic managers. The traffic managers voluntarily made these reductions for two reasons. First, each of them sought, by lowering his rates, to capture business from competitors. Competitive rate-making has now been greatly reduced—although not wholly eliminated—by railway combinations and consolidations and by legislation requiring the roads to publish all their rates, and to give extended notice of proposed changes. The second reason why the traffic managers reduced rates was that they hoped thereby to develop so much additional traffic that the net returns from it on the lower rates would exceed the net returns from a smaller traffic on the higher rates. Often this hope was disappointed; then, whenever practicable, the old rates were restored. The desire to increase earnings is just as prevalent and strong today as ever; and the traffic managers still manifest it not only by raising the rates on commodities the volume of whose movement they think will not thereby be reduced, but also by reducing them on commodities the volume of whose movement they think will thereby be largely increased. They seek constantly to make that adjustment which will yield the railway the largest permanent return, and they know that in the long run they will get the largest return by making no rates that are lower, and none that are higher, than the traffic easily can bear. The enormous increase of traffic shows that, as a whole, the rates of American railways are not burdensome to commerce, but are admirably adapted to foster its growth.

Now, it is obvious that limitation of profits would deprive the traffic manager of every railway which was earning a "fair return" of all incentive voluntarily to make reductions in rates. At present if the traffic manager has a movement of empty cars in one direction, and a shipper convinces him that by making a certain reduction in rates he can develop traffic that will fill

his empty cars and add something more to his road's earnings than to its expenses, he will promptly make the reduction. But under a policy of limiting profits he would not be keen to experiment with reductions in rates, for he would know that if he did not develop as much traffic as he expected to, and a loss of net earnings resulted, it would have to be borne by the railway, while if an increase of net earnings resulted, it would be wiped out by further reductions of rates by public authorities.

It may be answered that if the traffic managers did not make reductions the regulating authorities would. But it has never yet been demonstrated that the railways, as a whole, are now earning more than a fair return on a fair valuation. Most of those who have studied the subject believe that a fair valuation would show that to reproduce the railways of the country as a whole would cost much more than their present aggregate capitalization.¹¹ Now, the net earnings of the railways as a whole do not exceed the average current rate of interest on their present aggregate capitalization. The dividends declared in 1908, applied to all the stock outstanding, averaged only 5 per cent. On the theory of a "fair return on a fair valuation" general reductions in rates by the regulating authorities probably could not now be justified. And if the conclusion reached in a previous part of this paper is correct—viz., that this policy would tend to reduce the enterprise of railway management, and thereby to increase expenses of operation—it probably would make it impossible for regulating authorities to require general reductions, and, on the other hand, render it possible for the railways, on the ground that they were not earning a "fair return," legally to make even greater general advances than they are now seeking to justify on the ground of increasing expenses of operation.

¹¹ Their net capitalization in 1908, according to the Interstate Commerce Commission, was \$12,840,091,462. United States Senator A. B. Cummins, of Iowa, is an advocate of limitation of profits, yet in a speech before the Traffic Club of Chicago on February 8, 1910, he said he believed a valuation would show it would cost \$20,000,000,000 to reproduce the physical properties of the railways. He therefore opposes a valuation. He contends that railways are not entitled to the "unearned increment" in their properties.

It may be replied that while the railways as a whole are not earning excessive profits, there are some that are; and that while the policy of limitation of profits might not lead to general reduction of rates, or even prevent general advances, it at least would prevent advances and justify reductions on those roads which are earning more than a "fair return." Hitherto in this paper I have treated the railways of this country as if they were a single system. The fact that they are not, far from making the carrying out of the policy of limitation of profits through regulation of rates more feasible and expedient, makes it much less so. For railways vary as widely in their abilities and characteristics as the men who manage them. In every section there are some whose traffic is relatively heavy, whose operating expenses are relatively small, and whose net earnings per mile are relatively large. In the same sections there are other roads whose traffic is relatively light, whose operating expenses are relatively large, and whose net earnings are relatively small. Everywhere these two classes of roads compete for business. They must make the same rates or the road which makes the lowest rates will get all of the competitive business; and therefore if the regulating authorities so reduced or held down the rates of the stronger roads as to limit their profits to a "fair return" the weaker roads would be restricted to less than a "fair return." If the rates of the stronger roads, such as the Pennsylvania, the Lake Shore & Michigan Southern, the Burlington, the Chicago & Northwestern, the Louisville & Nashville, and the Union Pacific, should be so held down or lowered as to restrict their net earnings to the current rate of interest, the net earnings of other roads would be reduced much below it, and many would be bankrupted.

The policy of governmental control and limitation of profits through regulation of rates does not seem well adapted to secure any of the main objects of regulation of railways. It appears to be more apt to injure than to benefit the public. The most equitable, effective, and beneficial way to determine and fix reasonable rates is to proceed in much the same way

that the courts determined what was a reasonable rate under the common law. When an individual rate or a schedule of rates is in question, whether that rate or schedule is fair and reasonable cannot be determined merely by reference to how much profit the railway is making in the aggregate. For if the road's profits were small, it might be held that the rate or schedule was reasonable; whereas the fact might be that the particular rate or schedule in question was excessive and that the smallness of the road's profits was due to the excessiveness of this rate or schedule, or to the lowness of its other rates, or to bad management. And if its profits were large it might be held that the particular rate or schedule in question was excessive; whereas the fact might be that that rate or schedule actually was unfairly low and that the road's profits were all derived from other and higher rates. Similarly, if the large profits of a single road were considered, it might be held that its rates were excessive; whereas investigation might disclose that other roads hauling the same kinds and amounts of traffic, under substantially similar conditions, for the same rates, were making small or no profits; which would show that the differences in profits were mainly or entirely due to differences in the skill of the managements. The Interstate Commerce Commission said in one of its opinions in *Central Yellow Pine Association v. Illinois Central Railroad Co., et. al.* (10 I. C. C. 539):

While the Supreme Court has undertaken to point out "certain elements" to be considered in determining the reasonableness of an entire system of rates, it has not named any as shedding light upon the reasonableness of a rate on a single commodity like lumber. It is evident that such elements are widely variant in the two cases. Where an entire system of rates is involved, the principal, if not the only question is, whether the revenue yielded by the rates on all traffic is a fair return on the value of that which is "employed for the public convenience"—a question, the determination of which, as we have shown, can have only a very remote, if any practical bearing on the reasonableness of a rate on a single article of traffic. On the other hand, where the rate on a single article is in issue, the question (which could not arise in the former case), whether the rate is unjustly discriminatory or unduly preferential, may be presented, and the reasonableness of the rate depends upon the value, volume, and other characteris-

tics affecting the transportation of the particular commodity to which it is applied.

And again:

The rate on one article of traffic may be reasonably high and the carrier fail to earn a fair return on the value of the entire property employed for the public convenience because of unreasonably low rates on other traffic, and vice versa, the rate on one article of traffic may be unremunerative or unreasonably low and the return to the carrier from its entire business may be fair or reasonably high, the deficiency under the rate on the one article of traffic being made up by the rates on the balance of the traffic.

Some consideration ought and must be given to their profits in determining what rates railways should be allowed to charge. But there should also be considered the nature of the services rendered; their value to the shippers receiving them; how the profits of the railways affected compare with those of other industrial concerns in the same territory; the density and nature of the traffic; how much the traffic can reasonably bear; how much other railways than those involved charge for similar services and earn on similar rates, etc. If, in view of these considerations, the rates seem unreasonably high *per se* they should be reduced; and if they seem unreasonably low *per se* they should be allowed to be advanced. The courts have held that railways cannot charge extortionate rates *per se*, even if they cannot otherwise make any profit; and it would seem that if they do make reasonable rates it is neither equitable nor expedient to reduce their rates merely because their profits are large. It would seem that the most effective way to get low rates would be not to provide that the reasonableness of a railway's rates should be measured by the amount of its profits, and that the greater its earnings grew the lower it would have to make its rates, but to provide, if some practicable way of carrying out such a plan could be devised, that the reasonableness of the profits should be measured by the reasonableness of the rates, and that the *lower* a road made its rates the larger should be the profits that it would be allowed to enjoy.

SAMUEL O. DUNN